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S E C R E T SECTION 01 OF 03 RIYADH 000910

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FOR SECRETARY GEITHNER FROM AMBASSADOR ERDMAN  
LONDON PASS TO TREASURY SECRETARY

E.O. 12958: DECL: 07/12/2019  
TAGS: [ECON](#) [PREL](#) [EAID](#) [EFIN](#) [EINV](#) [KTFN](#) [PINR](#) [OVIP](#) [SA](#)  
SUBJECT: SCENESETTER FOR TREASURY SECRETARY GEITHNER'S JULY  
14 VISIT TO SAUDI ARABIA

Classified By: CDA Ambassador Richard Erdman for reasons 1.4 (b) and (d)  
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#### INTRODUCTION

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11. (S) Embassy Riyadh warmly welcomes you to the Kingdom. While it's not exactly magical, it is unique and it is important. Unique because it's the only country in the world that is named after the ruling family and where almost all the senior government positions are filled by either brothers or half-brothers of the founder of "modern" Saudi Arabia, King Abdulaziz. And important because Saudi Arabia, by virtue of its energy resources, financial power, counterterrorism efforts, and leadership of the Muslim world, plays a critical role in almost every global and regional issue of importance to us.

12. (S/NF) The good news is that the Saudi leadership sees the United States as its most important strategic partner and guarantor of its stability. In addition, we generally have shared objectives on global and regional issues, whether it is a matter of global financial and energy stability, threats posed by terrorism and extremism, the urgent need for progress toward Middle East peace, or the dangers posed by Iran and destabilization in Pakistan. The bad news is that we not infrequently differ on tactics, we see the King sometimes as unduly cautious when bold leadership is required (as in Middle East peace efforts), and the King sees us as not always reliable, consistent, or willing to heed their advice on critical issues such as Iraq. Added to the mix, of course, is that our cultures and value systems at home could not be more different, and this ensures a degree of built-in tension, skepticism, and hesitancy in the relationship.

#### ESTABLISHING PERSONAL TRUST IS KEY

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13. (S/NF) Your most important meeting here, needless to say, will be with King Abdullah who is shortly to turn 86, remains in reasonably good health, but works only a few hours every day. In the highly centralized Saudi decision-making system, no decision of any importance is or can be made without the King's personal approval. In this regard, the most important thing to know about the King is that, true to his Bedouin roots, character, honesty, and trust are everything in his forming judgments about foreign leaders. He expects commitments to be respected and sees actions, not words, as the true test of commitment; and he expects good-faith

consultations, not surprises. If you don't enjoy that trust, as is the case with Maliki, Zardari, and Bashar Al-Asad, it's hard to change minds. But if you do have it -- and the establishment of a warm, personal bond with the President was arguably the most important concrete result of his recent visit -- many things become possible, even if there are differences along the way. At a minimum, it guarantees a fair hearing of one's views.

14. (S) Apart from the King and various princes accompanying him, you will also be meeting with some of his most trusted advisers. Finance Minister Ibrahim Al-Assaf, a non-royal with a PhD from the University of Denver, has the King's ear on economic issues and wields considerable power through his control of the various ministries' purse strings. Central Bank Governor Muhammed Al-Jasser, promoted to his current position this past February (having served as Vice Governor since 1995), strongly supports both the dollar-riyal peg and a conservative investment strategy. Recently, he has been pushing the country's financial sector to develop a corporate bond market as an alternative source of project finance.

#### KING ABDULLAH'S ECONOMIC AGENDA

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15. (S) Secretary Clinton has provided you helpful context and background on the key regional issues we have recently been discussing with the Saudis -- our hope for additional assistance to the Palestinian Authority; more relief assistance to internally displaced refugees in Pakistan; strengthened efforts against terrorist finance; a firm

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approach to Iran, even while seeking engagement; and cooperation in seeking to draw the Taliban away from al-Qaeda. So this message will focus on the Saudi economic context, agenda, and perspectives.

16. (S/NF) King Abdullah is deeply engaged on economic issues, personally chairing the Kingdom's highest economic coordinating body, the Supreme Economic Council. The King has an ambitious agenda, including economic diversification, investment promotion, and the provision of jobs for a Saudi youth bulge that is just now reaching maturity. To meet these goals, he has instituted a substantial array of reforms, carried out by a few trusted lieutenants. These reforms include the creation of a new investment promotion agency to overhaul the once-convoluted process of starting a business here, the creation of a regulatory body for capital markets, the construction of the King Abdullah University for Science and Technology (to be the country's flagship institution for higher education and research), and a substantial budgetary investment in educating the workforce for future jobs. The Kingdom's 2009 budget reflects these priorities -- 22 percent is devoted to education -- and amounts to a significant economic stimulus package.

#### ECONOMIC CONTEXT: PARTIALLY INSULATED

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17. (S) Since the inception of the global financial crisis in mid-2008, Saudi Arabia's economy has been somewhat insulated, more impacted by lower oil prices and tighter international credit than by exposure to toxic assets. Some individual investors have lost considerable sums in the Dubai real estate bubble collapse and in international equities markets. But the economy has slowed less than most others, mainly due to a rapid easing of monetary policy, increased provision of credit by the government, and falling raw materials prices in the construction sector. That said, recent loan defaults by three family conglomerates, with little warning to the banking sector, have cast some doubt on whether the full impact of global economic troubles has yet to arrive. Following these defaults, other merchant families are likely to encounter tighter credit conditions as local and international banks reassess risk in the absence of

transparency. The king will be interested in hearing your ideas on regulatory reform since he has been repeatedly critical of developed economies' lax oversight and has argued for increased regulation of financial flows.

SAUDI CONCERNS: INFLATION AND DIVERSIFICATION

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18. (S) Your visit comes at a pivotal moment for the Kingdom's economic recovery. Your Saudi counterparts, particularly central bank governor Al-Jasser and Finance Minister Al-Assaf, are certain to look to you for reassurance on issues that affect this recovery and Saudi Arabia's overall financial position -- namely, that U.S. debt is manageable, that we have a plan to bring government spending under control, and that we will continue to support the value of the dollar. Over the 20-year period leading up to the early 2000s, inflation in the Kingdom averaged less than two percent, but has increased sharply in the past three years. Imported inflation from dollar weakness through mid-2008 was a high-profile contributing factor. Inflationary pressure peaked in July 2008 at 11 percent, began to fall as oil prices declined and credit markets stalled, but has gathered steam again beginning this past May. Although unlikely in the short-term, Saudi officials could eventually consider revaluing their currency if a failure to do so means significantly greater inflation, and the accompanying social and political consequences, here in the Kingdom. De-pegging remains a remote possibility, though the Saudis are keeping an eye on what other major actors like China are doing. We expect Saudi officials would communicate their intentions in advance of taking any significant steps with respect to their currency regime.

19. (C) Over the past several years, the Saudis have devoted substantial time and attention to economic diversification, albeit with limited success. Despite the long potential

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lifespan of Saudi oil reserves relative to many of their neighbors (60-plus years by the most conservative estimates), last year's spike in oil prices, and the ensuing drop in global demand as consumers increased both conservation and the pursuit of alternatives, drove home to the Saudis the need to expand beyond petroleum and petrochemicals. To that end, the Saudi government is encouraging the development of other sectors in which they have a comparative advantage, including mining, solar energy, and religious tourism. Dovetailing closely with this are steps they have taken to improve their workforce through better, knowledge-based education. These steps include re-shuffling the Ministry of Education's leadership in February (bringing in the King's pro-reform son-in-law as the new minister) and devoting a quarter of their 2009 budget to education.

U.S. CONCERNS: TERRORISM FINANCE

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110. (S/NF) When the Department of the Treasury reopened its office in Riyadh in August 2008 after a 15-year gap, it represented an important avenue to increase pressure on Saudi authorities to step up efforts against terrorism finance. As a result of joint Treasury - GRPO teams identifying actionable information for the Saudis, as well as an increased appreciation on the part of the Saudis for the importance of counterterrorism finance, we are now seeing significant signs of progress. These include: increased information sharing, an increase in terror finance-related arrests, action against donors as well as facilitators, and the implementation of some regulatory reforms. Nevertheless, the Kingdom remains a significant source of funds for some terrorists, particularly groups like the Taliban and Hamas. Our main interlocutor on these issues, Assistant Interior Minister Muhammed bin Nayif (son of Interior Minister Prince Nayif), is out of the country. Nonetheless, it would be useful and appropriate, in your meeting with the King and/or

with others, to welcome the progress that has been made in this key area, encourage continued efforts to develop information on donors, and urge stepped up efforts to educate the public about extremist causes and to publicize convictions.

ERDMAN